

**NATIONAL
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OF FEDERAL
EMPLOYEES**

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SERVING FEDERAL EMPLOYEES AND THE NATION SINCE 1917

STATEMENT BY

THE NATIONAL FEDERATION OF FEDERAL EMPLOYEES

BEFORE

THE HOUSE POST OFFICE AND CIVIL SERVICE COMMITTEE

ON

THE DEVELOPMENT OF A SUPPLEMENTAL RETIREMENT SYSTEM

OCTOBER 23, 1985

Mr. Chairman and Subcommittee members:

I appreciate the opportunity to testify today on the development of a new supplemental retirement system for Federal employees hired after December 31, 1983. As the representative of over 150,000 civil servants, many of whom will be participants of the new plan, the National Federation of Federal Employees is deeply concerned about the Government's ability to meet its retirement obligation to both its new and current employees. Such a goal is especially important since the retirement annuity stands as the keystone of the Government's benefit package.

For the last two years, the Committee has undertaken one of the most comprehensive reviews of the Civil Service Retirement System (CSRS). The product of that study, a supplemental retirement plan for newly hired Federal employees, was recently unveiled by the Chairman and Subcommittee Chair Oakar. While the actual legislation has not been drafted, the outline presented to us suggests a program that could closely replicate the benefits of the current system. I must therefore congratulate both the Chairman and Representative Oakar for proposing the best supplemental system we have seen so far. You, along with your staff, are to be commended for making difficult decisions on the retirement future of the new Federal workforce.

The Committee has recognized that a retirement annuity is the most important job benefit an employee can earn -- a considera-

tion which is especially true for employees of the Federal Government. Thanks to successive pay caps and now a pay freeze, Federal pay is falling even further behind private sector salaries. Civil service retirement, on the other hand, is the only major benefit that compares favorably with similar programs in the private sector. As such, it is the primary incentive for individuals to enter the Federal workforce and to pursue a Government career. It cannot be overlooked as an important recruitment and retention tool. Maintaining a sound retirement system is therefore in the best interests of both the employees and the Government they serve.

Throughout the discussion of the Supplemental Retirement Plan, NFFE has urged Congress to develop a plan that replicates the benefits and costs of the current system as closely as possible. Certainly, it would be a mistake to create a plan with the sole criterion of balancing the budget. Cost savings should not be the primary factor in establishing the supplemental retirement system because the last thing we want is a cheap retirement plan. Likewise, we feel strongly that it would be a disaster to create a new system that did not continue to preserve the basic elements of the CSRS -- specifically early retirement, full cost-of-living adjustments and the high-3 salary formula.

The early retirement option, which has long been available to Federal employees, is perceived by the employees to be one of the most-valued retirement benefits available under the current

system. Eliminating the option for post-1983 employees would be both unnecessary and unfair. For a start, the existing age and service requirements have resulted in an average Federal retirement age that is close to that in the private industry. According to the General Accounting Office, civil servants retire at an average age of 61.1 with 29 years of service while their private sector counterparts retire at age 61.8. By penalizing new employees for exercising an option open to their peers, Congress would create two separate systems of age and service requirement. The NFFE firmly believes that new employees should have the same retirement option as current Federal workers.

However, this would not be the case under legislation the Senate Governmental Affairs Committee recently approved. The bill, S. 1527, establishes a three-tiered retirement system that restricts the early retirement option to employees who choose one of two alternatives. By dividing the new plan into two options, the bill in essence creates two separate systems. Not only would it be impossible to administer, it would also further fragment employees who would be faced with not two but three different retirement plans.

I am also concerned about the reduced cost-of-living adjustments retirees would receive under the Senate bill. Currently, Federal retirees are eligible for a full COLA. S. 1527 offers several different COLAs depending upon the employee's age and the option he or she chooses. Once again, this is confusing and unfair.

Reducing the COLA violates one of the most fundamental principles of a staff retirement plan - to protect annuitants from a loss in the value of their income replacement. On the basis of equity alone, the Supplemental Retirement Plan should provide full inflation adjustments.

In a further departure from the current system, S. 1527 seeks to modify the method of calculating annuities based on an employee's salary base. Currently, the formula is derived by using the highest average wages over a three-year period. Under the Senate bill, the salary base would be determined from an average of the highest five years, thus lowering an employee's base considerably. In addition to the lower accrual rates proposed for the new retirement plan, the high-5 would contribute to a significantly lower pension.

Realizing the importance of continuing these benefits, the Chairman and Representative Oakar have proposed a supplemental retirement system that would preserve early retirement, a full COLA and the high-3 salary formula. In addition, your proposal provides a social security supplement for employees who retire before they are old enough to collect their social security benefits. Without the supplement, retirees between the ages of 55 and 62 would be forced to live on meager annuities when they could least afford to do so. The failure to provide the interim financial support would also serve as a deterrent to early

retirement. As you have recognized, the supplement must be a component of any new plan.

The individuals who could really get lost in the early retirement shuffle are those who are required to retire from their jobs at a certain age. These Federal employees, considered special category employees, frequently place their lives in jeopardy or are subject to undue stress and pressures in the course of their duties. In recognition of these extraordinary pressures, the Government has afforded them additional retirement benefits - benefits which must not be forgotten in the establishment of a new retirement plan.

For the most part, special category employees appear to be well taken care of in the Senate bill and in your intended legislation. Both proposals seek to preserve the current age and service requirements and provide a supplement between Federal retirement and social security eligibility. However, there is still one category of employees whose special retirement needs have not been fully recognized in S. 1527. They are the civilian technicians employed by the National Guard.

Although the Government does not consider technicians to be special category employees, these civil servants are nevertheless frequently forced to retire before age 62. In order to maintain their civilian jobs, they must concurrently hold a military position. If the technician loses his military position, through

no fault of his own, he is automatically separated from his civilian job. Unfortunately, forced early separation is not an uncommon event.

For example, the selective retention boards which review the enlistment of all National Guard members with more than twenty years of military service are frequently the cause for separation. Since most technicians are veterans, they tend to achieve the service years by the time they reach age 50. Thus, a technician can find his military position terminated, for reasons unrelated to his civilian performance, at an early age. Because many technicians lose their jobs this way, it is essential that any new retirement plan provides them with a social security supplement. I commend the Chairman and Representative Oakar for presenting a system that would do just this. Under the proposal you have offered, all employees who retire after age 55 would be eligible for the social security supplement. I urge the remaining Committee members to embrace this essential benefit and to fully support it in conference.

I would now like to address the issue of the Capital Accumulation Plan which, aside from social security coverage, is the most significant change from the current system. While the concept of a CAP, or thrift plan, has merit, there are inherent difficulties associated with its application and administration. Since I have not seen any specific proposal concerning your proposed thrift plan, Mr. Chairman, I will address my comments to the CAP

envisioned by S. 1527 and to the general needs a thrift plan should meet.

Q The plan approved by the Senate Governmental Affairs Committee leaves me with four immediate concerns. They are: the effective management of potentially vast sums of money and their impact on the economy; the creation of a new Government entity with appointees who more than likely do not have the necessary expertise to administer the thrift plan funds; the strong economic power base of such individuals; and finally, the restriction of an employee's fundamental right to choose where his or her retirement investments should be made.

As more and more employees join the Federal workforce and participate in the thrift plan, a huge sum of money will be available for investment. In fact, the fund will be the largest single employer-thrift fund in the world and as such could have a significant impact on the economy. As the funds accrue, they could increase to such monumental proportions as to be completely unwieldy and possibly economically threatening. While it is true that private pension funds now hold approximately \$1.3 trillion and absorb \$100 billion a year, the funds are held by individual pension funds. There is no single board which decides how these monies are invested.

Under S. 1527, however, a single board would be established to set the investment policy and to make decisions controlling what

will amount to several hundred billion dollars annually. As you can imagine, the potential economic power the thrift board would have would be enormous. Additionally, political and financial manipulation would be a constant threat. Safeguards against such manipulation could never be made strong enough. Even if Congress legislated protections, there is no guarantee that the protections would be sufficient.

The size of the Government entity required to actually administer the thrift plan proposed by S. 1527 would have to be enormous if the right management and investment decisions were to be made. I do not believe that the investment board or the advisory committee can adequately meet these responsibilities. Not only would it be difficult to attract the high caliber employees needed to fulfill such a mandate, but appointed officials with little or no investment experience would be making the final decisions. I am not confident that the best decisions would be made. The Federal Government should not even be in the business of making this type of investment decision.

Finally, the Senate thrift plan fails to give employees adequate control over their retirement account. Although the plan provides its participants with instruments in which to invest their funds, it takes away their independence to make such decisions for themselves. The Capital Accumulation Plan, therefore, cannot be considered an adequate investment vehicle.

I firmly believe that any new Federal thrift plan must enable, even encourage, employees to make their own investment decisions to suit their individual retirement needs. You would do a great injustice to Civil Servants if you underestimated or limited their ability to determine their own retirement investments. The Federal workforce today is better educated and more professional than at any other time in its history. So it is only fair that its employees be given the right to control their own retirement future.

Federal employees have been shut out of the debate over their compensation package far too long. Unlike their private sector counterparts, they are unable to negotiate over the benefits that ultimately affect their pocketbooks. The difference is especially evident in the retirement area where private sector unions play an active roll in pension and thrift plans. But now we have the opportunity to bring employees into this debate by giving them the right to actively participate in their retirement future. The Committee could do this by allowing employees to designate the retirement accounts in which their funds will be invested. Such an approach would eliminate the need for a new Government entity that would have invested the money into Government-established accounts. The number of participating plans could be restricted, such as health plans are in the Federal Employees Health Benefits Program, to qualified thrift accounts sponsored by employee organizations. In this way, the employee could take

advantage of the highest yield thrift accounts that would meet established standards.

Since the contributions will be placed into individual thrift accounts, no Federal body would be needed to make the investment decisions. Authority to promulgate regulations whereby thrift accounts may be established, qualified and implemented could be given to the Department of the Treasury or another Federal agency. Such regulations would be submitted to the appropriate House and Senate Committees for review and approval no later than sixty days after the date of enactment.

Once the employee designates a qualified investment account, the amount contributed by the employee and employer would be deposited to the credit of the participant. Investments under any such program could include securities, guaranteed income securities, Federally-insured deposits or accounts, and other options, including investments in pooled funds, not specifically disapproved by regulation. The employee could specify the amount to be deducted from each paycheck and the tax-deferred employee and matching employer contributions would then be electronically transferred and deposited into the thrift account.

Any participant for whom an account is established and maintained could elect to change such designations at least once annually. Information relating to the status of the participant's account would be provided at least semi-annually to the employee or

his/her beneficiary. A summary plan description and fund prospectus should also be provided.

The chosen investment account would have to comply with such regulations as the appropriate Federal agency prescribed to safeguard the interests of the participants and their beneficiaries. The Department of the Treasury could assume some of these responsibilities. It could also be given the authority to bring a civil action to seek an injunction or to obtain other equitable relief.

The thrift plan could be phased in by requiring the employee's CAP contribution to be held in Government securities for a period not to exceed twelve months. The lag would give the Government time to establish the necessary regulations and safeguards, while allowing the participants sufficient time to choose their investment option. It would also give employee organizations time to establish qualified plans. As provided by S. 1527, participants who contributed toward the interim plan between January 1, 1984 and the effective date of the thrift plan would receive credit toward the CAP for their own contributions, the employer's matching contribution plus interest on the aggregate amount. Such funds could be invested in Government securities until the effective date of the plan.

After the "initiation period" expires, 100 percent of the employee's post-1983 contribution would be invested into the designated account and not automatically invested in Government

securities as S. 1527 stipulates (unless the employee specifically designates). The investment in Government securities required by the Senate bill would, of course, have an immediate beneficial impact on the deficit. So it is hard for me to believe that, once the deficit reduction has been realized, the employee will ever be given the opportunity to invest outside of the Government.

My concerns are magnified by the direction Congress is taking on the Gramm-Rudman balanced budget amendment. If the President is ever given the authority to "sequester" funds to meet annual budget cuts of at least \$36 billion, there is no doubt in my mind that he will turn to the new supplemental retirement thrift fund and require the Government's money to stay on budget permanently. If the Government seeks immediate deficit reduction benefits, it can instead invest its own matching contribution in Government securities for a given period of time before investing entirely in the account of the employee's choice. The schedule specified in S. 1527 provides one alternative.

<u>Contributions in cal. year</u>	<u>Required to be in Gov't Securities</u>
<u>Employer</u>	
1986	N/A
1987	100%
1988	100
1989	100
1990	100
1991	100
1992	100
1993	80
1994	60
1995	40
1996	20

The design of a retirement plan that encompasses both a defined benefit, defined contribution and social system is a formidable task. The supplemental plan that you have proposed appears to have dealt with the major concerns raised in the debate over establishing the new system. It is my hope, therefore, that you will not close the supplemental system to current employees. Although you allow them to participate in the thrift plan, you preclude any freedom of choice to transfer completely. As I mentioned earlier, Federal employees today are well-educated and far from naive. If Congress creates a supplemental retirement plan that better suits their needs, then Congress should also grant pre-1984 employees the right to switch into that plan.

In conclusion, Mr. Chairman, I commend both you and Representative Oakar for your efforts to develop the best possible supplemental system. Your proposal appears to protect both the current and new employees by maintaining age and service requirements, full inflation protection and sound disability and survivor

benefits. I hope that your peers will also recognize the merits of your supplemental retirement plan and join you in sponsoring it.

That concludes my statement Mr. Chairman. I am happy to answer any questions you may have.